



**DEFENSE CONTRACT AUDIT AGENCY**  
**DEPARTMENT OF DEFENSE**  
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IN REPLY REFER TO

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MEMORANDUM FOR REGIONAL DIRECTORS, DCAA  
DIRECTOR, FIELD DETACHMENT, DCAA  
HEADS OF PRINCIPAL STAFF ELEMENTS, HQ, DCAA

SUBJECT: Audit Alert on Professional and Consultant Service Costs (FAR 31.205-33) and  
Purchased Labor

**This guidance is effective immediately for all new and in-process assignments.**

**Why are we issuing this guidance?**

Based on input from field audit offices, internal quality assessments, and inquiries from DCMA, we recognize a need to emphasize audit guidance on the evidence necessary to satisfy the FAR 31.205-33(f) documentation requirements for professional and consultant services. In addition, we want to ensure that when testing a transaction for allowability, we apply the appropriate audit criteria (i.e., FAR Cost Principle) based on the nature of the claimed cost and not the account in which the contractor recorded the cost. In some instances, costs recorded as consultants may represent purchased labor, and audit teams should evaluate these costs using appropriate audit criteria. The enclosed Frequently Asked Questions (FAQs) provide several scenarios to assist in implementing this guidance.

**What are the documentation requirements of FAR 31.205-33(f)?**

FAR 31.205-33(f) contains three documentation requirements to ensure that professional and consultant service costs can be determined allowable: (1) details of all agreements; (2) invoices or billings; and (3) consultant work product and related documents. Auditor judgment is critically important in determining whether the totality of the evidence demonstrates the nature and scope of the services provided. We have to assure ourselves that there is an agreement between the contractor and the consultant, we have to see the invoices, and we have to be able to determine the output from the consultant to assess the propriety and legality (i.e., allowability) of the consultant services. The type of evidence satisfying the documentation requirements will vary significantly based on the type of consulting effort and from contractor to contractor. Therefore, it is important for the audit team to understand that the evidence required from the contractor is essentially the following:

- An agreement that explains what the consultant will be doing for the contractor;
- A copy of the bill for the actual services rendered, including sufficient evidence as to the time expended and nature of the services provided to determine what was done in

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exchange for the payment requested, and that the terms of the agreement were met. This documentation does not need to be included on the actual invoice and can be supported by other evidence provided by the contractor;

- Explanation of what the consultant accomplished for the fees paid – this could be information on the invoice, a drawing, a power point presentation, or some other evidence of the service provided.

The claimed costs are unallowable without evidence of an agreement, an invoice, and what work the consultant actually performed. It is important to clarify that the audit team is looking for evidence to satisfy these three areas and not a specific set of documents. Therefore, auditor judgment will be the determining factor on the type and sufficiency of evidence required to satisfy these requirements.

The audit team should explain to the contractor that they are looking for evidence that a prudent person would already possess (i.e., understand what they are buying, how much they will pay, and ensure they receive what they paid for), and should not call for the creation of documentation.

The contractor may provide evidence created when the contractor incurred the cost as well as evidence from a later period. Audit teams should consider evidence from a later period provided by the contractor, taking care to assess the quality of the evidence (generally, evidence prepared after the fact is less persuasive) and will likely need to obtain additional corroborative evidence. As an example of evidence from a later period, the contractor may facilitate a meeting between the consultant and the audit team to obtain documentation (oral/written) from the consultant regarding what effort they performed (i.e., third party confirmation). The audit team should consider the evidence provided by the consultant, along with other evidence obtained, to determine if the total evidence gathered is sufficient to satisfy the documentation requirements.

**Are there any special concerns related to the work product requirement in FAR 31.205-33(f)(3)?**

The purpose of the work product requirement is for the contractor to be able to demonstrate what work the consultant actually performed (in contrast to what work is planned to be performed). Although a work product usually satisfies this requirement, other evidence also may suffice. Therefore, if the audit team has sufficient evidence demonstrating the nature and scope of the consultant work actually performed, the contractor has met the FAR 31.205-33(f)(3) requirements even if the actual work product (e.g., an attorney's advice to the contractor) is not provided. The audit team should not insist on a work product if other evidence provided is sufficient to determine the nature and scope of the actual work performed by the consultant.

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**When do you apply the documentation requirements in FAR 31.205-33(f)?**

FAR 31.205-33(a) defines professional and consulting services costs as services rendered by persons who are members of a particular profession or possess a special skill and who are not officers or employees of the contractor. Examples include those services acquired by contractors to enhance their legal, economic, financial, or technical position. Audit teams must first determine whether the underlying nature of the claimed cost represents professional and consultant services before applying the documentation requirement in FAR 31.205-33(f).

**Should you apply the documentation requirements in FAR 31.205-33(f) to all costs claimed in the account titled “Consultants”?**

The audit team’s assessment of the underlying nature of the claimed costs determines whether FAR 31.205-33 is applicable and not the contractor’s accounting classification. For instance, contractors may record expenses for purchased labor (e.g., janitorial, clerical, security) in a “Consultant” or “Professional Services” account; this does not make these costs subject to the requirements of FAR 31.205-33. Likewise, costs recorded in other accounts may be professional and consultant service costs and the auditor should evaluate the costs using the criteria of FAR 31.205-33.

**What FAR requirements should the audit team apply to purchased labor?**

FAR does not have a specific cost principle covering purchased labor. However, the contractor should have adequate documentation to support the reasonableness of amounts paid, demonstrate the person who provided the service, and evidence that the effort represented allowable activities. If the audit team determines the payment was not reasonable for the services performed (FAR 31.201-3, Determining Reasonableness), or the contractor made payment without adequate support that the person provided the service (FAR 31.201-2d Determining Allowability), the audit team should question the costs under the appropriate provision of FAR.

The contractor may record purchased labor as direct, indirect, or a combination and may reflect them in various cost categories (e.g., direct labor, subcontract, or overhead). CAM Section 7-2102 provides additional guidance on purchased labor.

**Should we always cite FAR 31.205-33 as the non-compliance resulting in the questioned cost?**

If the audit team obtains only part of the evidence required by FAR 31.205-33(f), and the audit team determines from the evidence that the activity performed by the consultant is unallowable based on another provision of FAR, the audit team should question the cost, citing the specific provision first (e.g., FAR 31.205-1, Public Relations and Advertising Costs), followed by a discussion of how the requirements of FAR 31.205-33(f) were not met.

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In cases where the FAR 31.205-33(f) documentation requirements are met, but the consultant costs are unallowable based on another provision of FAR, the costs should be questioned by citing just the specific provision (e.g., FAR 31.205-1, Public Relations and Advertising Costs), and not citing FAR 31.205-33(f).

In cases where the audit team cannot gather sufficient documentation to support the evidence requirements of FAR 31.205-33(f), but other evidence leads the team to conclude the activity is an otherwise allowable activity and reasonable in amount, the team should cite the FAR 31.205-33(f) non-compliance and question the cost. In the audit report note, the team should include a discussion of the evidence supporting why the activity is otherwise allowable and reasonable in amount, so that the contracting officer can make a fully informed business decision.

#### **Are there any consultants who require special treatment?**

Provided the services rendered meet the FAR 31.205-33(a) definition (i.e., services by a professional or specially skilled person to enhance their legal, economic, financial, or technical position of the contractor), the cost should be reviewed under FAR 31.205-33 and then, based on that assessment, ensure that the activity is not unallowable under any other FAR provision. Contractors often argue that attorney-client privilege protects documentation of work performed by attorneys; however, this is not the case. Refer to CAM 1-504.4g for resolving contractor assertions of attorney-client privilege or attorney-client work product doctrine.

#### **Questions and Further Information**

FAO personnel should direct questions to their regional points-of-contact, and regional personnel should contact Policy Accounting and Cost Principles at (703) 767-3250 or by e-mail at [DCAA-PAC@dcaa.mil](mailto:DCAA-PAC@dcaa.mil).

/Signed/

Donald J. McKenzie  
Assistant Director  
Policy and Plans

Enclosure:

Frequently Asked Questions

DISTRIBUTION: E

## FREQUENTLY ASKED QUESTIONS

**Question 1:** A contractor uses a temporary accounting service to perform bookkeeping activities. The accounting service provided several individuals to input vendor invoices into the contractor's accounts payable system after the buyers approved them for payment. Are these costs professional and consultant services?

**Answer:** No. Accounting, by any reasonable interpretation, is a profession under the FAR 31.205-33(a) definition. However, the type and nature of the work performed in this example represents clerical effort that is not a professional and consultant service. Accordingly, it would not be appropriate to evaluate these costs using FAR 31.205-33 criteria. Since these costs represent purchased labor, the audit team should consider the guidance relating to purchased labor discussed above.

**Question 2:** The contractor enters into an agreement with an individual to perform program management activities for one of its contracts. In this capacity, the individual worked directly with contractor employees and contractor management to track and monitor progress on contract performance. Is this a consultant and should the audit team require documentation consistent with the FAR 31.205-33(f) criteria?

**Answer:** No. In this circumstance, the individual is equivalent to a contractor employee. The contractor integrated the individual as an inherent part of operations and no single work product exists to demonstrate the effort expended. The individual's contribution was to the overall management of contract performance. Accordingly, it would not be appropriate to evaluate these costs using FAR 31.205-33 criteria. Since these costs represent purchased labor, the audit team should consider the guidance relating to purchased labor discussed above.

**Question 3:** The contractor hired a thermal engineer to address a program-specific technical issue. The contractor charges the costs direct to the benefitting CAS-covered contract. The extent of technical input required was significant and the value of the agreement is over \$1 Million. Should the audit team use the criteria in FAR 31.205-33 to evaluate these costs?

**Answer:** The individual possesses a specialized skill and provides a service to enhance the technical capability of the contractor consistent with the FAR 31.205-33(a) definition. Accordingly, the contractor has appropriately classified the thermal engineer as a consultant. Whether the contractor charges the costs direct or indirect does not affect whether the costs meet the FAR 31.205-33(a) definition. In addition to applying the documentation requirements in FAR 31.205-33(f), the audit team should evaluate the contractor's approach for selecting and compensating the consultant to ensure that the amounts are reasonable. FAR 31.205-33(d) provides considerations for determining allowability including:

- Qualifications of the individual or concern rendering the service and the customary fee charged, especially on non-Government contracts.
- Adequacy of the contractual agreement for the service (e.g., description of the service, estimate of time required, rate of compensation, termination provisions).

## FREQUENTLY ASKED QUESTIONS

**Question 4:** The contractor engages an efficiency engineer to evaluate the design of the manufacturing process. The contractor classifies the engineer as a consultant and provided documentation supporting the claimed amounts. Our initial fieldwork found that both the agreement and the billings submitted by the engineer clearly satisfy the FAR 31.205-33(f) requirements. However, the documentation for work product is limited to a single agenda item from an executive meeting where the contractor contends the engineer verbally presented his recommendations (which the contractor asserts they adopted). Is this sufficient evidence of work product to accept these costs?

**Answer:** No, but the audit team should apply alternate audit procedures to collect other corroborative evidence. One example would be if the contractor demonstrates action taken to revise the manufacturing process tied directly to the consultant's recommendations. Other corroborative evidence may include the auditor's physical inspection of the contractor's manufacturing facility identifying the recommended improvements, interviews with the contractor employees involved in the manufacturing process, and coordination with a DCMA technical specialist or Government program office technical support staff.

**Question 5:** The contractor provides an agreement and invoices in support of claimed consultant costs as part of an incurred cost audit. The contractor does not have evidence supporting the consultant's work product, but offers to obtain a letter from the consultant describing the work performed, which in this case involved attending technical meetings with Air Force program officials. The contractor further indicates the same Air Force officials are still on the program and will be visiting next week to discuss follow-on effort. The contractor offers to set up a meeting with the Air Force officials to permit the auditors to confirm the consultant's participation. Should the audit team consider the consultant letter and meet with the program officials as part of their determination of the allowability of the consultant costs?

**Answer:** The audit team should consider the consultant's testimonial evidence and should meet with the Air Force program officials. The testimonial evidence provided by the consultant is similar to a third party confirmation (i.e., evidence from outside the contractor's organization). However, since it was prepared several years after-the-fact, it may not be sufficient on its own. The meeting with the Air Force program officials corroborates the contractor and consultant assertions and provides an independent confirmation. In this case, the audit team should consider the sufficiency and appropriateness of all evidence (contemporaneous and from a later period) in reaching a conclusion. If the audit team was unable to corroborate the testimonial evidence of the consultant with the Air Force program officials, they should consider other appropriate audit procedures, such as having the contractor arrange a meeting with the consultant to confirm legitimacy (i.e., the consultant actually exists) and to gather additional evidence regarding the actual work performed by the consultant.

**Question 6:** The contractor hires an international marketing consultant to evaluate and recommend new areas to promote, sell, and distribute products (market planning activities). The agreement provides for a \$12,000 monthly flat-fee payment. In submitting invoices, the consultant references the agreement and details the actual services provided. However, the billings do not include details on the number of hours worked. Should the audit team question these costs under FAR 31.205-33(f)(2) because the invoices do not detail the time expended?

## FREQUENTLY ASKED QUESTIONS

**Answer:** The audit team should not automatically question the consultant costs simply because the invoice does not detail the time expended. The audit team should first review the billings in combination with the terms of the agreement. Then meet with the contractor to ascertain what other evidence the contractor can provide to determine if the payment is consistent with the services agreed to and provided. Further testing should determine the nature and scope of the services planned and actually performed to ensure the allowability of the costs. The auditor also should ensure the amount paid is reasonable for the services performed and sufficient evidence exists to establish that the consultant performed the services.

**Question 7:** A consultant provided a training course to the contractor's pricing group on how to prepare proposals that comply with the requirements of FAR Part 15. The contractor provided a copy of the agreement and the paid invoice. The contractor also provided a list of attendees, but the contractor does not have a copy of the training material used by the consultant to serve as evidence of work product. Should the audit team question the consultant costs due to lack of documentation?

**Answer:** Not necessarily. The agreement, paid invoice, and some evidence that the class was actually given is sufficient to satisfy the FAR 31.205-33(f) requirements. The audit team could further support that the class occurred by collecting testimonial evidence through interviews conducted with employees listed as attendees.

**Question 8:** The contractor's incurred cost claim includes expenses paid to a public relations firm hired to improve the company's image. The contractor booked the costs as a consultant and, in support of the claimed amounts, provided an agreement, billings, and work product. The agreement describes in detail the work requirements, rates of compensation, etc. The invoice billings include sufficient detail as to the time expended and the nature of the actual services provided. The work product includes trip reports, weekly memoranda of activities completed, and a final report. Since the contractor met all of the documentation requirements, is the claimed cost allowable?

**Answer:** No. Notwithstanding the meticulous documentation provided by the contractor for this consultant, the underlying costs are unallowable under FAR 31.205-1, Public relations and advertising costs. In evaluating the nature of the services for allowability, the audit team should consider the unallowable activities identified in FAR 31.205-33(c) as well as the provisions of other cost principles, as applicable (e.g., FAR 31.205-22, Lobbying and political activity costs; FAR 31.205-27, Organization costs; FAR 31.205-47, Costs related to legal and other proceedings; FAR 31.205-38, Selling costs).

**Question 9:** The contractor uses outside writers to augment their in-house staff in preparing technical publications and we are unsure whether they are consultants or not. The contractor's staff prepares drafts of the manuals focusing on technical content. The outside writers proofread the drafts and make recommendations to improve readability.

## **FREQUENTLY ASKED QUESTIONS**

**Answer:** Since the effort performed by the outside writers does not enhance the contractor's legal, economic, financial, or technical position, they do not meet the definition of a consultant. Since these costs represent purchased labor, the audit team should consider the guidance relating to purchased labor discussed above.